

The Investment Analysts Journal

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Die Beleggings- ontleiders Tydskrif

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This issue in brief

The influence of political news events on share market activity in South Africa

The aim of this paper is to investigate the relationship between domestic political news events and share market activity on the Johannesburg Stock Exchange as measured by volume traded and the price volatility of a number of share indices. From the popular press it appears as though business analysts, editors and reporters believe that political events exert an influence on financial markets. This is especially true in South Africa, where political reporting has reigned supreme for a number of years. The country has gone through a period of transition, which started with the release of Nelson Mandela in 1990 and climaxed with the first fully democratic election in 1994. This transition period was characterised by political uncertainties, violence on the one extreme and bouts of optimism on the other extreme. The influence of these political events on the Johannesburg Stock Exchange (JSE) were often highlighted in articles like the following, which have appeared in the local press during 1994.

Assessing portfolio performance: The case of South African Unit Trusts

The standard approach used to assess the performance of unit trust managers is based on the premise that the investment strategy is basically stationary. Active management is viewed as being confined to timing – occasional switching between risky and riskless securities – and selectivity – switching between securities of essentially the same systematic risk to exploit temporary mispricing. This research utilises a traditional measure of portfolio performance and a relatively straightforward methodology that attempts to identify the timing and selection skills of a sample of South African unit trust managers.

The effect of industrial strikes on the value of shares listed on the Johannesburg Stock Exchange

The objective of this study is to determine the effect of strikes on the share values of a sample of companies listed on the Johannesburg Stock Exchange during the period 1984-1993. The results indicate that strikes do have a negative effect on share prices. The costs of a strike do not appear to be transitory since the losses incurred during the strike period are not counterbalanced by positive excess returns after its conclusion. The findings tend to support the notion that capital markets are usually able to anticipate whether an impending contract deadline will result in a strike or settlement. In the prestrike period, however, the stock market consistently underestimates the cost of a strike to shareholders, as demonstrated by the fact that nearly 70% of the total decline of returns (3,64%) occurs after the strike is announced.

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Futures-Trading Activity and Share Price Volatility in South Africa

The study examines the relationship between futures-trading activity and equity volatility on the JSE for the three main indices. Contrary to findings in other markets, it is shown that positive correlation exists between equity volatility and expected and unexpected trading volumes in both the spot and futures markets. These conclusions seem robust to alternative specifications and indices used. Given an assumption of causality which runs from futures trading volumes to spot market volatility, the results are consistent with the idea that increasing trade in the futures market lead to greater volatility and price destabilisation in the share market.

The Determinants of the Risk Perceptions of Investors

The ultimate test of theory is whether it explains real world behaviour. In recent years, serious doubts have arisen as to the ability of the Capital Asset Pricing Model (CAPM) to explain investor behaviour. It has been argued that a study of investor risk perceptions will provide a different perspective on the investment and valuation process. The objective of this study was to explore investor risk perceptions and to identify how investors treat risk in practice. The CAPM presumes that rational investors strive to maximise wealth, and it seeks to explain the relationship between risk and return, as well as to provide a mechanism for evaluating required rates of return on investments in risky assets. The CAPM is based on the premise that investors are principally concerned with those risks they cannot eliminate through diversification. This non-diversifiable risk is also termed market risk or systematic risk and stems from the 'market' factor, that is the influence of the general economic environment on investments. The CAPM provides an explicit measure of systematic risk, namely beta. Numerous authors have questioned the assumptions regarding the decision making behaviour of investors on which this theory is based, and estimation problems have been identified with beta. Thus there has been an erosion of confidence in the model, and this has led researchers to conclude that, despite efforts to improve the measurement of beta, "its usefulness to investment professionals has reached a plateau and that investors are looking elsewhere for measures, or additional measures, of risk" (Mear and Firth, 1988, p335). Partly in response to the criticisms of the CAPM, researchers have sought alternative approaches to the valuation process and to measuring risk. Two major alternatives have emerged, namely microeconomic modelling and the use of a behavioural science approach.

The Investment Analysts Journal

Forty-fourth issue – Summer 1996/7

The performance of share prices on the Johannesburg Stock Exchange in 1996 has been bewildering in a number of respects. In the first place, Wall Street has risen impressively and this is something that in the past has strongly influenced Diagonal Street. Secondly, the rand has been devalued by almost twenty-five per cent against the dollar. Historically, when that has happened, there has usually been a strong rise in both mining and industrial share prices. Thirdly, economic growth in the US has been good encouraging the prospect of a wider recovery in the economies of South Africa's leading trading partners. The business cycle in this country generally lags the overseas business cycle by between six and eighteen months so the prospects seems reasonable that growth by the end of 1997, or in the first half of 1998 at the latest, will be in an upswing again. In the meantime, real GDP here is still projected to increase by at least 2,5 per cent. Stock market prices are supposed to be leading indicators, not lagging ones. Fourthly, the government has presented a sensible macroeconomic strategy to both domestic and foreign investors and this has even been given a nod of approval by the IMF. Why then all the pessimism?

Of course when share prices are down there are always explanations and these are not difficult to find in present circumstances. For example, noises coming from the political arena have been worrying. Just when everybody had adjusted to the prospect of Thabo Mbeki succeeding Mr Mandela when the latter steps down in 1999, the President drops a bombshell to the effect that he has not selected Mr Mbeki as his heir. This, if it was not calculated to do so, has certainly raised concerns of a political power struggle in the ANC as 1999 approaches. Right now South Africa needs an ANC power struggle at national level as much as the Free State needed such a struggle at provincial level. Not only did the latter struggle damage the party's credibility and reputation as a professional and disciplined organisation, it also affected the process of government in the province adversely. An ANC power struggle at national level would justifiably invite the gravest of concerns in the minds of investors everywhere. Africa's record of such struggles is not the best and the concerns of investors would range all the way to the possibility of a resurgence of political violence such as that which only recently dominated the situation in Natal. We do not need to go further north in Africa for horrific examples in this regard.

Another troubling factor has been the dissension within the ANC-COSATU-SACP alliance over the government's new macroeconomic strategy. COSATU's criticisms of the strategy, and its rejection of its central objective regarding the reduction of the deficit before borrowing in particular, have been a concern. With debt servicing costs now the second largest item on the government's expenditure budget, and rapidly approaching the education budget in size, one is forced to wonder as to what kind of logic drives its macroeconomic thinking. Of course, reducing the deficit involves problems, and downsizing in the public sector is one of them. But is COSATU seriously arguing that jobs can be saved in the long run by casting fiscal

Die Beleggings-ontleders Tydskrif

Vier-en-veertigste uitgawe – Somer 1996/7

Die vertoning van aandelepryse op die Johannesburgse Aandelebeurs in 1996 het in verskeie opsigte verras. In die eerste plek het die pryse op Wall Street indrukwekkend gestyg – iets wat in die verlede altyd 'n sterk invloed op Diagonaalstraat gehad het. In die tweede plek het die rand met byna vyf en twintig persent teenoor die dollar gedevalueer. Wanneer so iets in die verlede gebeur het, het sowel die myn- as nywerheidsaandele gewoonlik sterk geklim. In die derde plek het die goeie ekonomiese groei in die VSA die moontlikheid vergroot dat die ekonomieë van Suid-Afrika se belangrikste handelsvennote aan 'n breër front sou herstel. Omdat die sakesiklus in hierdie land gewoonlik tussen ses en agtien maande agter die oorsese sakesiklus is, is die vooruitsig redelik goed dat daar teen die einde van 1997 of op die laaste in die eerste helfte van 1998 weer 'n opswaai in die groei sal wees. Intussen word steeds 'n toename van 2,5 persent in die BBP hier geprojekteer. Pryse op die aandelebeurse is veronderstel om leidende aanwysers te wees wat nie sloer nie. In die vierde plek het die regering 'n heel verstandige makro-ekonomiese strategie aan sowel die binnelandse as buidelandse beleggers voorgedra wat selfs deur die IMF goedgekeur is. Maar waarom is almal dan so pessimisties?

Vir dalende aandelepryse is daar altyd verklarings, wat in die huidige omstandighede nie moeilik is om te vind nie. Uit byvoorbeeld die politieke arena klink daar sekere geluide op wat allermens gerusstellend is. Net toe almal gewoon begin raak aan die gedagte dat adj. pres. Thabo Mbeki mnr. Nelson Mandela sal opvolg wanneer laasgenoemde in 1999 uitree, krap die President sake lelik deurmekaar deur te kenne te gee dat hy mnr. Mbeki nog nie as sy opvolger "gesalf" het nie. Hoewel dit miskien nie so bedoel was nie, het dit vrese laat ontstaan oor 'n politieke magstryd in die ANC rondom 1999. Op die oomblik kan Suid-Afrika net so min 'n ANC magstryd op nasionale vlak bekostig as 'wat die Vrystaat dit op provinsiale vlak nodig het. Die stryd in die Vrystaat plaas nie net 'n vraagteken oor die party se geloofwaardigheid en goeie naam as 'n professionele en gedissiplineerde organisasie nie, maar dit ry ook die regeringsproses in die provinsie in die wiele. 'n ANC magstryd op nasionale vlak sal tereg tot ernstige kommer lei onder alle beleggers. Afrika se rekord in hierdie verband lyk nie al te goed nie en besorgde beleggers kan selfs begin dink aan die moontlike opvlaming van die politieke geweld wat nog onlangs die toneel in KwaZulu-Natal oorheers het. Ons hoef ook nie baie verder noord in Afrika te soek na afskuwelike voorbeelde hiervan nie.

Nog 'n onrusbarende faktor is die tweespalt in die ANC-COSATU-SACP alliansie oor die regering se nuwe makro-ekonomiese strategie. COSATU se kritiek op die strategie en in die besonder sy verwerping van die allerbelangrike doelwit om die tekort voor verdere lenings te verminder, is 'n bron van kommer. Dat die skulddelgingskoste nou die naasgrootste item op die regering se uitgawebegroting is en in omvang vinnig die onderwysbegroting inhaal, laat 'n mens wonder oor die logika agter sy makro-ekonomiese denke. Om die tekort te verminder gaan vanselfsprekend

caution to the winds? Or is it only interested in the short run, and the jobs of its members as apposed to the well-being of the wider population? In this regard, the matter of inflation deserves special mention. Has COSATU one might ask, ever stopped to think of the damage this does to the masses of ordinary people, most of them black and poor, who save their hard earned money in fixed income repositories and then, when their savings are not sufficient to meet their old age requirements, are thrown onto the assistance of the State. The very State whose burgeoning deficit is generating the inflation in the first place? Jobs created or jobs saved through the printing of money cannot be sustained in the long or even medium run. There is no other answer but to get the dissaving of the public sector down, deliberately and surely, even if that means tempering ones action to take account of destabilising political effects. The dogmatic rejection of any possibility of a further raising of VAT, indeed the threat of general strike at the very suggestion of the matter, when such a move actually makes a great deal of fiscal sense, is hardly calculated to inspire confidence in the government's ability to follow through with its macroeconomic proposals.

Finally, there is the matter of the rand exchange rate and the role the Reserve Bank has been playing to halt its decline. If speculators are right in seeing the Bank as a net buyer of rand at any particular time, they must also be right in concluding that the rand would be lower than it is were the Bank not in the market to support it. And this would be true even were the rand actually to be oversold on any consideration of economic fundamentals. Keynes made the point a long time ago but it deserves repeating regarding the behaviour of speculative markets generally. 'It happens,' said Keynes, 'that the energies and skill of the professional investor and speculator are ... largely concerned, not with making superior long-term forecasts of the probable yield of an investment over its whole life, but with foreseeing changes in the conventional basis of valuation a short time ahead of the general public. They are concerned, not with what on investment is really worth to a man who buys it "for keeps", but with what the market will value it at, under the influence of mass psychology, three months or a year hence. Moreover, this behaviour is not the outcome of a wrongheaded propensity. It is the inevitable result of an investment market organised along the lines described. For it is not sensible to pay 25 for an investment of which you believe the prospective yield to justify a value of 30, if you also believe that the market will value it at 20 three months hence.' If confidence in the rand is to be restored, two things are essential. First, the adverse inflation differential between South Africa and its leading trading partners must be eliminated. Second, the rand must be allowed to find its own level in exchange markets. Moreover, these two requirements are inter-linked. When the adverse differential has been eliminated, the rand's own level will not be a cause of fear to the South African monetary authorities. And when it is at its own level, concerns of prospective investors that it might be forced lower by negative speculation will logically be less, encouraging their long-term direct commitments.

A matter of some interest to an assessment of current stock market performance is the failure of both the mining and industrial sectors to respond to the decline that has occurred in the rand exchange rate since February. When the financial rand was in existence, a fall of 25 per cent in the exchange rate was usually accompanied by a firming of share prices. That has not happened on this occasion and the question is 'Why?' A number of possible answers

met sekere probleme gepaard, waarvan die afskaling van die openbare sektor een is. Maar dink COSATU eerlik- waar dat die diensstaat op langtermyn verklein kan word deur fiskale dissipline oorboord te gooi? Of stel hy slegs in die korttermyn belang, en in werkgeleenthede vir sy eie lede in plaas van vir die breë bevolking? In hierdie verband verdien die kwessie van inflasie spesiale aandag. 'n Mens kan jou afvra of COSATU al ooit gedink het aan die implikasies hiervan vir die menigte gewone mense, van wie die meeste swart en minder bevoorreg is, wat hul swaarverdiende geld in vaste deposito's belê het en wat, indien hul spaargeld dan ontoereikend vir hul behoeftes blyk te wees, op hul oudag op hulp van die staat aangewese sal wees. Dit is die einste staat wie se groter wordende tekort in eerste instansie vir inflasie verantwoordelik was. Daar kan nie op langtermyn of selfs op mediumtermyn voortgegaan word met die skepping van werkgeleenthede of die besnoeiing van poste deur bloot geldnote te laat druk nie. Die enigste oplossing is om die ontsparing van die openbare sektor doelbewus en doelgerig te verlaag, selfs al moet 'n mens die maatreëls verwater om met destabiliserende politieke gevolge rekening te hou. 'n Kategoriese afwysing van enige moontlikheid om die BTW-koers verder te verhoog – die blote gedagte daaraan sal begroet word met 'n dreigement van 'n algehele staking, hoewel so 'n stap fisikaal sinvol sal wees – is hoegenaamd nie bedoel om vertroue te kweek in die regering se vermoë om met sy makroekonomiese voorstelle deur te druk nie.

In laaste instansie is daar die kwessie van die randwisselkoers en die rol wat die Reserwebank speel om hierdie daling te stuit. Indien spekulate korrek is in hul siening van die Bank as 'n netto koper van rand op enige spesifieke tydstip, kom hulle seker ook tot die logiese gevolgtrekking dat die rand nog swakker sou gewees het as die Bank dit nie in die mark gedra het nie. Dit sou moontlik kon wees selfs indien te veel rand inderdaad bloot op grond van ekonomiese beginsels verkoop is. 'n Stelling wat Keynes lank gelede gemaak het, kan ook hier op die gedrag van spekulatiewe marke oor die algemeen van toepassing gemaak word: "It happens," said Keynes, "that the energies and skill of the professional investor and speculator are ... largely concerned, not with making superior long-term forecasts of the probable yield of an investment over its whole life, but with foreseeing changes in the conventional basis of valuation a short time ahead of the general public. They are concerned, not with what an investment is really worth to a man who buys it 'for keeps', but with what the market will value it at, under the influence of mass psychology, three months or a year hence. Moreover, this behaviour is not the outcome of a wrongheaded propensity. It is the inevitable result of an investment market organised along the lines described. For it is not sensible to pay 25 for an investment of which you believe the prospective yield to justify a value of 30, if you also believe that the market will value it at 20 three months hence." Twee dinge is nodig om vertroue in die rand te herstel. Ten eerste moet die nadelige inflasiedifferensiaal tussen Suid-Afrika en sy vernaamste handelsverrekte uit die weg geruim word. Ten tweede moet die rand toegelaat word om sy eie vlak in die valutamarkte te vind. Hierdie twee vereistes is ook onderling verbind. Wanneer die nadelige verskil uit die weg geruim is, sal die rand se eie vlak nie 'n bron van kommer vir die Suid-Afrikaanse monetêre owerheid wees nie. En wanneer dit op sy eie vlak is, sal dit vanselfsprekend in 'n mate die yrese besweer van voornemende beleggers dat dit deur negatiewe spekulasie nóg laer gedwing sal word en hulle dan tot direkte langtermynverbintnisse oorhaal.

suggest themselves. One is that an upward correction in share prices has been delayed. Another is that a new situation has come into effect in which classical adjustment responses no longer apply and that the market is now set upon uncharted waters. Given the major political changes that have taken place in South Africa since 1994, and most particularly the opening of the South African economy to the world economy that has occurred in terms of ANC economic policy (the removal of exchange control with respect to non-residents, the lowering of tariff barriers in terms of GATT, deregulation of financial markets and prospective privatisation), the possibility is real that a completely new investment situation is in the process of coming into place. If this is the case, competition in the equity market can be expected to increase making portfolio management different and more challenging from anything that has been experienced in the days of the hothouse economy of yesteryear. It is a challenge investment analysts will need to take seriously if they are personally to survive in career terms and if their profession is to play its proper part in helping the country to realise its true and undoubted potential.

THE EDITOR

Wat interessant in die beoordeling van die aandeelbeurs se huidige vertoning is, is dat die myn- en nywerheidssektor nie reageer op die daling wat sedert Februarie in die randwisselkoers plaasvind nie. In die tyd van die finansiële rand het 'n daling van 25 persent in die wisselkoers gewoonlik gepaardgegaan met 'n verstewiging van die aandeelpryse. Dit was nie hierdie keer die geval nie. Waarom nie? 'n Mens kan aan 'n paar moontlike redes dink, onder meer dat 'n opwaartse regstelling in aandeelpryse vertraag is en dat 'n nuwe situasie hom voordoen waarin klassieke aanpassings nie langer geld nie en die mark hom nou op 'n onbevare see bevind. Teen die agtergrond van die ingrypende politieke veranderinge sedert 1994 in Suid-Afrika en in die besonder die oopstelling van die Suid-Afrikaanse ekonomie aan die wêreld ekonomie ingevolge die ANC se ekonomiese beleid (die opheffing van valutabeheer ten opsigte van nie-Suid-Afrikaanse burgers, die verlaging van tariefmure volgens die AOTH, die deregulering van die geldmarkte en die voorgename privatisering), is dit 'n wesenlike moontlikheid dat 'n geheel en al nuwe beleggingsituasie aan't ontstaan is. In so 'n geval kan toenemende mededinging op die aandelemark verwag word, wat portefeuljebestuur nie net sal verander nie, maar ook 'n groter uitdaging sal maak as tydens die kweekhuis-ekonomie van vroeër. Dit is 'n uitdaging wat beleggingsontleders ernstig sal moet opneem as hulle persoonlik in hul loopbaan wil oorleef en ook as hul professie 'n wesenlike rol wil speel om die land te help om sy ware en onbetwyfelbare potensiaal te ontsluit.

DIE REDAKTEUR